



TAX EXEMPT AND
GOVERNMENT ENTITIES
DIVISION

DEPARTMENT OF THE TREASURY
INTERNAL REVENUE SERVICE
WASHINGTON, D.C. 20224

Number: **201114036**
Release Date: 4/8/2011

Date: January 11, 2011

UIL: 501.03-00

Contact Person:

Identification Number:

Contact Number:

Employer Identification Number:

Form Required To Be Filed:

Tax Years:

Dear :

This is our final determination that you do not qualify for exemption from Federal income tax as an organization described in Internal Revenue Code section 501(c)(3). Recently, we sent you a letter in response to your application that proposed an adverse determination. The letter explained the facts, law and rationale, and gave you 30 days to file a protest. Since we did not receive a protest within the requisite 30 days, the proposed adverse determination is now final.

You must file Federal income tax returns on the form and for the years listed above within 30 days of this letter, unless you request an extension of time to file. File the returns in accordance with their instructions, and do not send them to this office. Failure to file the returns timely may result in a penalty.

We will make this letter and our proposed adverse determination letter available for public inspection under Code section 6110, after deleting certain identifying information. Please read the enclosed Notice 437, *Notice of Intention to Disclose*, and review the two attached letters that show our proposed deletions. If you disagree with our proposed deletions, follow the instructions in Notice 437. If you agree with our deletions, you do not need to take any further action.

If you have any questions about this letter, please contact the person whose name and telephone number are shown in the heading of this letter. If you have any questions about your Federal income tax status and responsibilities, please contact IRS Customer Service at

1-800-829-1040 or the IRS Customer Service number for businesses, 1-800-829-4933. The IRS Customer Service number for people with hearing impairments is 1-800-829-4059.

Sincerely,

Holly Paz
Acting Director, Exempt Organizations
Rulings & Agreements

Enclosure
Notice 437
Redacted Proposed Adverse Determination Letter
Redacted Final Adverse Determination Letter



TAX EXEMPT AND
GOVERNMENT ENTITIES
DIVISION

DEPARTMENT OF THE TREASURY
INTERNAL REVENUE SERVICE
WASHINGTON, D.C. 20224

Date: November 26, 2010

Contact Person:

Identification Number:

Contact Number:

FAX Number:

UIL: 501.03-00

Employer Identification Number:

Legend:

President =

M =

N =

Date =

State =

Dear :

We have considered your application for recognition of exemption from Federal income tax under section 501(a) of the Internal Revenue Code (Code). Based on the information provided, we have concluded that you do not qualify for exemption under section 501(c)(3) of the Code. The basis for our conclusion is set forth below.

Facts:

You incorporated on Date in State and within a year, filed an application for recognition of exemption under section 501(c)(3) of the Code as a school described in sections 509(a)(1) and 170(b)(1)(A)(ii). Your President is located in Canada, one of your directors is in France and your other five directors are scattered throughout the U.S. Your primary source of revenue is loans from your President. You also receive donations, fees for research services, and conference sponsorships. Article II, Section B of your articles of incorporation states that:

The specific purpose of this corporation is to: the nonprofit provides collaboration, integration, and educational services to other universities, non-profits, and research organizations seeking to develop expertise in virtual organizational design and leadership. Our mandate is to research new methods of knowledge emergence, how those methods impact existing business models, and provide the necessary programs for public dissemination.

Article IV of your articles of incorporation states that:

This corporation is organized for charitable, religious, educational, and scientific purposes within the meaning of Section 501(c)(3), Internal Revenue Code,

including, for such purposes, the making of distributions to corporations that qualify as exempt corporations under section 501(c)(3) of the Code, or the corresponding section of any future federal tax code.

All of your activities are conducted in M or support M, a virtual collaborative environment (VCE). You stated that you stopped offering educational support services to organizations in exchange for fees, but continue to conduct the following activities:

1. Annual Conference. Within M, a virtual environment, you regularly organize and sponsor a conference where education and business entities within M can display their products and services to the public.
2. Basic and Advanced Classes. Within M, you offer free virtual basic entry-level classes about VCEs for members of M. You also offer a variety of virtual courses, including advanced 3D development, project management, and criminal justice for fees set at a level that will cover your costs. You also plan to offer a virtual executive master's program in virtual business strategy and organizational development for a fee.
3. Custom Educational Services. Within M, you offer organizations customized "on-demand" virtual educational services, including specialized VCE orientation programs, at established rates per student or group per hour. You are also currently negotiating with two universities to provide ongoing virtual orientation programs.
4. Forums. Within M, you conduct free virtual forums on subjects related to the development of VCEs and their impact on business and academia. For a fee, you also conduct virtual project management forums for professional recertification. You allocate at least 25 percent of your total time and resources to this activity.
5. Library/Peer review. Within M, you plan to offer online access to third party digital archives of journals, bibliographies, literature reviews, and articles. You will recover the cost of this access by either offering subscribers your reader card or by reselling the third party reader card. You also plan to publish an online quarterly peer review journal of academic papers related to VCEs that you will fund with subscription and advertising fees and sponsorships. You allocate at least 20 percent of your total time and resources to this activity.
6. Virtual Property management. Although you no longer offer virtual property management services to organizations on your website, you have not indicated that you will not honor your existing agreements to lease one virtual property to a university and manage 10 other virtual private estates within M.
7. Research. Within M, you plan to subsidize and support businesses and individuals that conduct research and development in the field of VCEs by providing publication, distribution and marketing services. You expect researchers to pay their own expenses. You allocate at least 10 percent of your total time and resources to this activity.

You state that, although there are approximately 300 VCE alternatives to M, you chose M as your primary "base of operations". You have no formal agreement with N, M's service provider, beyond the general terms of service to which all M registrants must agree. You plan to conduct a few programs in other virtual environments as part of your research and development activity.

You plan to take advantage of all opportunities to promote and market yourself within M and on your website. You promote all of your activities in M through word of mouth, student groups, and cross marketing with strategic partners. Within M, your two principal competitors are

section 501(c)(3) organizations that established their tax-exempt status outside of M, and subsequently expanded to offer services in M.

Law:

Section 501(c)(3) of the Internal Revenue Code (Code) provides for the exemption from federal income tax of organizations organized and operated exclusively for charitable, educational and other purposes, provided that no part of the net earnings inure to the benefit of any private shareholder or individual.

Section 1.501(c)(3)-1(a) of the Treasury Regulations (regulations) states that, in order to be exempt as an organization described in section 501(c)(3), an organization must be both organized and operated exclusively for one or more of the purposes specified in such section. If an organization fails to meet either the organizational test or the operational test, it is not exempt.

Section 1.501(c)(3)-1(b)(1)(i) of the regulations states that an organization is organized exclusively for one or more exempt purposes only if its articles of organization (a) limit the purposes of such organization to one or more exempt purposes, and (b) do not expressly empower the organization to engage, otherwise than as an insubstantial part of its activities, in activities which in themselves are not in furtherance of one or more exempt purposes.

Section 1.501(c)(3)-1(b)(1)(iii) of the regulations states that an organization is not organized exclusively for one or more exempt purposes if its articles expressly empower it to carry on, otherwise than as an insubstantial part of its activities, activities which are not in furtherance of one or more exempt purposes, even though such organization is, by the terms of such articles, created for a purpose that is no broader than the purposes specified in section 501(c)(3). Thus, an organization that is empowered by its articles "to engage in a manufacturing business" or, "to engage in the operation of a social club" does not meet the organizational test regardless of the fact that its articles may state that such organization is created "for charitable purposes within the meaning of section 501(c)(3) of the Code."

Section 1.501(c)(3)-1(b)(1)(iv) of the regulations states that in no case shall an organization be considered to be organized exclusively for one or more exempt purposes, if, by the terms of its articles, the purposes for which such organization is created are broader than the purposes specified in section 501(c)(3).

Section 1.501(c)(3)-1(c)(1) of the regulations states that an organization will be regarded as "operated exclusively" for one or more exempt purposes only if it engages primarily in activities which accomplish one or more of such exempt purposes specified in section 501(c)(3). An organization will not be so regarded if more than an insubstantial part of its activities is not in furtherance of an exempt purpose.

Section 1.501(c)(3)-1(d)(1)(i) of the regulations states, in part, that an organization may be exempt as an organization described in section 501(c)(3) if it is organized and operated exclusively for charitable or educational purposes.

Section 1.501(c)(3)-1(d)(1)(ii) of the regulations states that an organization is not organized or operated exclusively for one or more of the purposes specified in subdivision (i) of this subparagraph unless it serves a public rather than a private interest.

Section 1.501(c)(3)-1(d)(2) of the regulations states that the term "charitable" is used in section 501(c)(3) in its generally accepted legal sense and is, therefore, not to be construed as limited by the separate enumeration in section 501(c)(3) of other tax-exempt purposes which may fall within the broad outlines of "charity" as developed by judicial decisions. Such term includes: Relief of the poor and distressed or of the underprivileged; advancement of religion; advancement of education or science; erection or maintenance of public buildings, monuments, or works; lessening of the burdens of Government; and promotion of social welfare by organizations designed to accomplish any of the above purposes; or (i) to lessen neighborhood tensions; (ii) to eliminate prejudice and discrimination; (iii) to defend human and civil rights secured by law; or (iv) to combat community deterioration and juvenile delinquency.

Section 1.501(c)(3)-1(d)(3) of the regulations states, in part, that the term "educational" as used in section 501(c)(3), relates to the instruction or training of the individual for the purpose of improving or developing his capabilities, or the instruction of the public on subjects useful to the individual and beneficial to the community.

Section 1.501(c)(3)-1(d)(5) of the regulations states that since an organization may meet the requirements of section 501(c)(3) only if it serves a public rather than a private interest, a "scientific" organization must be organized and operated in the public interest. Therefore, the term "scientific", as used in section 501(c)(3) includes the carrying on of scientific research in the public interest. Research when taken alone is a word with various meanings; it is not synonymous with "scientific"; and the nature of particular research depends upon the purpose, which it serves.

Section 1.501(c)(3)-1(e)(1) of the regulations states that an organization may meet the requirements of section 501(c)(3) although it operates a trade or business as a substantial part of its activities, if the operation of such trade or business is in furtherance of the organization's exempt purposes or purposes and if the organization is not organized or operated for the primary purpose of carrying on an unrelated trade or business, as defined in section 513.

Rev. Rul. 68-71, 1968-1 C.B. 249 held that an organization that helped people in planning their careers and achieving occupational adjustment by distributing educational publications at a nominal charge and providing free vocational counseling services was exempt.

Rev. Rul. 68-504, 1968-2 C.B. 211, describes an organization formed to conduct an educational program for bank employees in a particular urban area. The organization furnished classrooms and employed local university professors and specialists in banking law to teach courses on various banking subjects. Membership in the organization is open to employees of all banks in the area. Citing section 1.501(c)(3)-1(d)(3) of the regulations, the ruling held that the organization qualified for exemption as an organization described in section 501(c)(3) of the Code.

Rev. Rul. 70-186, 1970-1 C.B. 128, describes an organization that preserved and improved a lake for public recreation. Lake front property owners and members of the community adjacent to the lake and municipalities bordering the lake financed the organization with contributions.

The ruling held that since the organization ensured the continued use of the lake for public recreational purposes, it was performing a charitable activity and was exempt under section 501(c)(3) of the Code. The benefits derived from the organization's activities flowed principally to the public through the maintenance and improvement of public recreational facilities, and any private benefits derived by the lake front property owners did not lessen the public benefits flowing from the organization's operations.

Rev. Rul. 74-116, 1974-1 C.B. 127 held that an organization whose membership is limited to organizations that own, rent or use a specific type of computer and whose activities are designed to keep members informed of current scientific and technical data of special interest to them as users of the computer was not exempt under Code section 501(c)(3).

Rev. Rul. 74-366, 1974-2 C. B. 345 held that the primary function of an organization that operated a summer camp for children and adults was not the presentation of formal instruction but the operation of a summer camp that involved both recreational and educational activities. The ruling also concluded that the counselor/trainee program was so interrelated with the other activities and facilities of the overall camp program that the trainee program could not be considered a school operated as an activity of the organization. The trainees learned primarily through experience by becoming involved in the camp activities.

Rev. Rul. 75-286, 1975-2 C.B. 210 held that a nonprofit organization with membership limited to the residents and business operators within a city block and formed to preserve and beautify the public areas in the block, thereby benefiting the community as a whole as well as enhancing the members' property rights, will not qualify for exemption under section 501(c)(3) of the Code, but may qualify under section 501(c)(4). The restricted nature of its membership and the limited area in which its improvements are made, indicate that the organization is organized to serve the direct private interests of its members within the meaning of section 1.501(c)(3)-1(d)(1)(ii) of the regulations.

Rev. Rul. 76-152, 1976-1 C.B. 151 held that a nonprofit organization formed by art patrons to promote community understanding of modern art trends by selecting for exhibit, exhibiting, and selling art works of local artists, retaining a commission on sales less than customary commercial charges and not sufficient to cover the cost of operating the gallery, did not qualify for exemption under section 501(c)(3) of the Code.

Rev. Rul. 76-206, 1976-1 C.B. 154, held that a nonprofit organization that was formed to generate interest in the classical music programs of a local for profit radio station was not exempt. The organization aided the for-profit program by seeking program sponsors, encouraging continuing support from existing sponsors, and by various other means to aid the radio station. Such activities tended to increase the revenues of the radio station. The organization's board did not include any representatives of the radio station. The Service held that where an education organization is serving both public and private interests, the private benefit must be clearly incidental to the overriding public interest.

Rev. Rul. 77-4, 1977-1 C.B. 141 held that an organization whose only activities were preparing and publishing a newspaper of local, national, and international news articles with an ethnic emphasis, soliciting advertising and selling subscriptions to that newspaper in a manner indistinguishable from ordinary commercial publishing practices, did not qualify for recognition of exemption under section 501(c)(3) of the Code.

In Better Business Bureau of Washington, D.C. v. U.S., 326 U.S. 279, 283 (1945), the Supreme Court held that the "presence of a single . . . [nonexempt] purpose, if substantial in nature, will destroy the exemption regardless of the number or importance of truly . . . [exempt] purposes."

In B.S.W. Group, Inc. v. Commissioner, 70 T.C. 352 (1978), the tax court found that a corporation formed to provide consulting services was not exempt under section 501(c)(3) because its activities constituted the conduct of a trade or business that is ordinarily carried on by for-profit commercial businesses. Its primary purpose was not charitable, educational, nor scientific, but commercial. The court found that the corporation failed to demonstrate that its services were not in competition with commercial businesses.

In American Institute for Economic Research v. United States, 302 F. 2d 934, 157 Ct. Cl. 548 (Ct. Cl. 1962), the claims court considered an organization that provided analyses of securities and industries and of the economic climate in general. It sold subscriptions to various periodicals and services providing advice for purchases of individual securities. The court noted that education is a broad concept, and assumed *arguendo* that the organization had an educational purpose. However, the totality of the organization's activities, which included the sale of many publications as well as the sale of advice for a fee to individuals, was indicative of a business. Therefore, the court held that the organization had a significant non-exempt commercial purpose that was not incidental to the educational purpose, and was not entitled to be regarded as exempt.

In Arlie Foundation v. Commissioner, 283 F. Supp. 2d 58 (D.D.C., 2003), the district court found that the organization was formed principally to organize, host, conduct and sponsor educational and other charitable functions on its facilities. The organization paid significant advertising and promotional expenses and derived substantial income from events held at its conference center. The court determined that the organization's activities competed with a number of commercial, as well as non-commercial entities, which strongly evidenced a commercial nature and purpose.

Among the major factors courts have considered in assessing commerciality are competition with for profit commercial entities; extent and degree of below cost services provided; pricing policies; and reasonableness of financial reserves. Additional factors include, *inter alia*, whether the organization uses commercial promotion methods (e.g. advertising) and the extent to which the organization receives charitable donations.

Thus, the court looked at the business methods of the organization as a method of inferring whether its purpose was to serve the public or whether there was a substantial non-exempt purpose of operating a business for profit.

In American Campaign Academy v. Commissioner, 992 T.C. 1053 (1989), the court held that an organization that operated a school to train individuals for careers as political campaign professionals, but that could not establish that it operated on a nonpartisan basis, did not exclusively serve purposes described in section 501(c)(3) of the Code because it also served private interests more than incidentally. The court found that the organization was created and funded by persons affiliated with Republican Party entities and that most of the organization's graduates worked in campaigns for Republican candidates. Consequently, the court concluded that the organization conducted its educational activities with the objective of benefiting

Republican candidates and entities. Although the candidates and entities benefited were not organization "insiders", the court stated the conferral of benefits on disinterested persons who are not members of a charitable class might cause an organization to serve a private interest within the meaning of section 1.501(c)(3)-1(d)(ii) of the regulations. The court concluded by stating that even if the Republican candidates and entities did "comprise a charitable class, the organization would bear the burden of proving that its activities benefited members of the class in a non-select manner."

Analysis and Conclusion:

An organization that is recognized as an organization described in section 501(c)(3) of the Code must be both organized and operated exclusively for exempt purposes. If an applicant fails to meet either the organizational test or the operational test described in section 1.501(c)(3)-1(a)(1) of the regulations, it is not exempt. The information you provided shows that you failed to meet both the organizational and the operational tests. Therefore, you are not exempt under section 501(c)(3) of the Code.

To be organized exclusively for one or more exempt purposes, an organization's articles of organization must limit its purposes to one or more exempt purposes, and must not expressly empower the organization to engage, other than as an insubstantial part of its activities, in activities which do not further one or more exempt purposes. See sections 1.501(c)(3)-1(b)(1)(i), (iii) and (iv) of the regulations. Your governing documents state that your specific purpose is to provide non-profit collaboration, integration, and educational services to other universities, non-profit organizations, and research organizations seeking to develop expertise in virtual organizational design and leadership. Your articles expressly empower you to engage, as a substantial part of your activities, in the provision of services to organizations. This activity does not further one or more exempt purposes. Therefore, you do not meet the organizational test.

An organization must engage primarily in activities that accomplish one or more exempt purposes to pass the operational test. See section 1.501(c)(3)-1(c)(1) of the regulations. You fail the first condition of the operational test because you do not primarily engage in activities that accomplish one or more exempt purposes.

Charitable Activities

An organization may be recognized as described in section 501(c)(3) of the Code if it is primarily organized and operated for charitable purposes. The Service recognizes charities as exempt because they benefit either the community as a whole or members of a charitable class. Providing services of an ordinary commercial nature in a community, even though the undertaking is beneficial to the community, is not regarded as conferring a charitable benefit on the community unless the service directly accomplishes a tax-exempt purpose. See section 1.501(c)(3)-1(d)(2) of the regulations. You provide services within M, which is a for-profit business, not a community. The types of services that you provide are primarily ordinary commercial activities, which, absent special circumstances, do not qualify as charitable activities. For example, your activities might be charitable if you provided services to members of a charitable class such as the poor or the underprivileged, but only if you provide such assistance in a charitable manner. You provide services to any member of M and the

introduction of a fee charge raises substantial doubts that you operate primarily for charitable purposes.

Educational Activities

An organization may be recognized as described in section 501(c)(3) of the Code if it is organized and operated exclusively for educational purposes. Section 1.501(c)(3)-1(d)(3) of the regulations states that the term "educational," as used in section 501(c)(3), relates to: (a) the instruction or training of the individual for the purpose of improving or developing his capabilities; or (b) the instruction of the public on subjects useful to the individual and beneficial to the community. Examples of educational organizations under the regulations include colleges and primary schools, public discussion groups that have panels, correspondence schools, and museums, zoos, and similar organizations. Since your basic VCE classes and general discussion forums relate to the instruction or training of individuals for the purpose of improving and developing their capabilities, you engage in some educational activities. However, you conduct many other noneducational activities.

Some of the noneducational activities that you conduct are offering custom educational services to organizations at established rates per hour/per student, managing virtual property for organizations for a fee, selling subscriptions to third party archives and your peer review journal, providing support services to researchers and organizing and sponsoring an annual conference for organizations that are members of M. These activities do not meet the definition of "educational" within the meaning of the regulations. See B.S.W. Group, Inc. v. Commissioner, and Rev. Rul. 77-4, *supra*. You are similar to the organization described in Rev. Rul. 74-366, *supra*, because your educational activities are so interrelated with your noneducational activities that we cannot conclude that you are operating exclusively for educational purposes.

Scientific Activities

An organization may be recognized as an organization described in section 501(c)(3) of the Code if it is organized and operated for scientific purposes. Section 1.501(c)(3)-1(d)(5) of the regulations states, in part, that the term "scientific" in section 501(c)(3) of the Code includes the carrying on of scientific research in the public interest. Research when taken alone is a word with various meanings; it is not synonymous with "scientific"; and the nature of particular research depends upon the purpose that it serves. You do not directly "carry on" or publish your own research. You promote and provide support services to researchers who will pay their own expenses. Since promoting and providing support services to researchers are not activities that meet the definition of "scientific research" in the regulations, we cannot conclude that you are operating exclusively for scientific purposes.

Providing Services for a Fee is a Commercial Purpose

Generally, providing services on a regular basis for fees is a trade or business ordinarily carried on for profit and is not an activity that is substantially related to any exempt purpose except insofar as it provides revenue. Organizations that operate a trade or business as a substantial part of their activities will only meet the requirements of section 501(c)(3) of the Code if the activity relates to and furthers an exempt purpose. Section 1.501(c)(3)-1(e)(1) of the regulations. Although you stopped offering educational support services to organizations, you continue to offer custom educational services to organizations at established rates per hour/per

student, virtual property management to organizations for a fee, peer review services and research support services, and you organize and sponsor an annual conference for organizations that are members of M. To meet the requirements of section 501(c)(3), these activities must be substantially related to one or more exempt purposes.

Several courts have considered whether organizations that conducted a trade or business furthered public or private, commercial purposes. In B.S.W. Group, Inc. v. Commissioner, *supra*, a corporation formed to provide consulting services was held not exempt under section 501(c)(3) of the Code because its activities constituted the conduct of a trade or business that is ordinarily carried on by commercial ventures organized for profit. The factors that the court relied upon included the corporation's failure to demonstrate that its services were not in competition with commercial businesses, the organization's financing, which did not resemble that of a typical section 501(c)(3) organization, the organization's failure to solicit and lack of voluntary contributions from the general public, and the fact that the corporation's only source of income was from fees for services and the fees were set high enough to recoup all costs. The court in Arlie Foundation v. Commissioner, *supra*, concluded that an organization operated for a non-exempt commercial purpose because of the commercial manner in which the organization conducted its activities. The court looked at factors including competition with for-profit commercial entities, the extent and degree of below cost services provided, the pricing policies, and the reasonableness of financial reserves. You are similar to these organizations because you have not shown that you do not compete with organizations that offer similar services, your primary source of revenue is loans from your President, your fees are set to recoup your costs, and you take advantage of all opportunities to market and promote your services.

In American Institute for Economic Research v. United States, *supra*, the court concluded that an organization's sales of publications were more analogous to commerce than to education and that its business purpose was primary and not incidental to its educational purpose. The court noted that in order for the organization to obtain its "contributions," it proffered something valuable in return. This necessity or purpose to provide such information and service as would be desired by the public placed the organization in competition with other commercial organizations providing similar services. Since the organization chose to compete in this manner, its activities acquired a commercial hue. Similarly, you plan to offer services and information to generate revenue, which places you in competition with commercial organizations that provide similar services. Because you allocate over a third of your time and resources to these activities, you devote a substantial part of your activities to operating a trade or business that is unrelated to any exempt purpose. In Better Business Bureau of Washington, D.C., Inc. v. United States, *supra*, the Supreme Court held that the presence of a single non-exempt purpose, if substantial in nature, will destroy the exemption regardless of the number or importance of truly exempt purposes. You failed the first condition of the operational test that requires an exempt organization to engage primarily in exempt activities because you operate for a substantial private, commercial purpose. See section 1.501(c)(3)-1(c)(i) of the regulations.

Private Benefit

An organization that serves a public interest and also serves a private interest other than incidentally, is not entitled to exemption under section 501(c)(3) of the Code. This statement supports the basic principle underlying the enforcement of charitable trusts and their exemption from income taxation under section 501(c)(3). Their property is devoted to purposes that are considered beneficial to the community in general, rather than particular individuals. See IV A.

Scott on Trusts, section 348 (3d ed. 1967) Thus, although an organization's operations may be deemed to be beneficial to the public, if it also serves private interests other than incidentally, it is not entitled to exemption. The word "incidental" has both qualitative and quantitative connotations.

Some exempt organizations provide qualitatively incidental benefits to private interests. For example, the organization described in Rev. Rul. 70-186, *supra*, maintained and improved public recreational facilities was exempt although, incidentally, some property owners derived a private benefit. Citing section 1.501(c)(3)-1(d)(3) of the regulations, the ruling held that the organization qualified for exemption as an organization described in section 501(c)(3) of the Code. Similarly, in Rev. Rul. 68-504, *supra*, an organization formed to conduct an educational program for bank employees that opened its membership to employees of all banks in the area was exempt. Compare to Rev. Rul. 74-116, *supra*, where an organization limited its membership to organizations that own, rent or use a specific type of computer and designed its activities to keep members informed of current scientific and technical data of special interest to them as users of the computer. The organization did not qualify for recognition of exemption under Code section 501(c)(3). See also Rev. Rul. 75-286, *supra*. Similarly, you limit your beneficiaries to M's members, restrict your activities to M and design your activities to keep members informed of current information related to VCEs, which is of special interest to them as users of M. In fact, you sponsor the annual conference to display the products and services of M's business and educational organizations. We recognize that, in an educational setting, some benefit to students and organizations is inevitable. However, like the organizations described in the last two rulings above, your restrictions provide an exclusive secondary benefit to M and M's members, which is not qualitatively incidental. See American Campaign Academy, *supra*.

Some exempt organizations provide quantitatively incidental benefits to private interests. To be quantitatively incidental, the benefit must be insubstantial in amount. For example Rev. Rul. 68-71, *supra*, held that an organization that helped people in planning their careers by distributing educational publications at a nominal charge and by providing free vocational counseling was exempt. Compare to Rev. Rul. 76-152, *supra*, that held that an organization formed to promote community understanding of modern art trends conducted an art sales activity that provided artists with direct monetary benefits and enhanced their careers, provided a substantial benefit and was not exempt. Similarly, you conduct all of your activities within M, and promote and market M and organizations that operate within M to the public, which increases M's membership and revenue. Because M would have had to purchase such promotion and marketing services itself, the benefit you provide M is substantial, and not quantitatively incidental. See also Rev. Rul. 76-206, *supra*.

Because you provide a substantial private benefit which is not qualitatively or quantitatively incidental to M and M's members, who are not members of a charitable class, you failed the operational test set forth in section 1.501(c)(3)-1(c)(1) of the regulations because you serve private interests other than incidentally.

Based on the information you provided, we are unable to conclude that you are organized and operated exclusively for the exempt purposes described in section 501(c)(3) of the Code. To be exempt, an organization must show that it is both organized and operated exclusively for one of more of the purposes described in section 501(c)(3). Section 1.501(c)(3)-1(a) of the

regulations. If an organization fails the organizational and operational tests described in the regulations, it is not exempt. You failed both tests.

You have the right to file a protest if you believe this determination is incorrect. To protest, you must submit a statement of your views and fully explain your reasoning. You must submit the statement, signed by one of your officers, within 30 days from the date of this letter. We will consider your statement and decide if the information affects our determination.

Your protest statement should be accompanied by the following declaration:

Under penalties of perjury, I declare that I have examined this protest statement, including accompanying documents, and, to the best of my knowledge and belief, the statement contains all the relevant facts, and such facts are true, correct, and complete.

You also have a right to request a conference to discuss your protest. This request should be made when you file your protest statement. An attorney, certified public accountant, or an individual enrolled to practice before the Internal Revenue Service may represent you. If you want representation during the conference procedures, you must file a proper power of attorney, Form 2848, *Power of Attorney and Declaration of Representative*, if you have not already done so. For more information about representation, see Publication 947, *Practice before the IRS and Power of Attorney*. All forms and publications mentioned in this letter can be found at www.irs.gov, Forms and Publications.

If you do not file a protest within 30 days, you will not be able to file a suit for declaratory judgment in court because the Internal Revenue Service (IRS) will consider the failure to protest as a failure to exhaust available administrative remedies. Code section 7428(b)(2) provides, in part, that a declaratory judgment or decree shall not be issued in any proceeding unless the Tax Court, the United States Court of Federal Claims, or the District Court of the United States for the District of Columbia determines that the organization involved has exhausted all of the administrative remedies available to it within the IRS.

If you do not intend to protest this determination, you do not need to take any further action. If we do not hear from you within 30 days, we will issue a final adverse determination letter. That letter will provide information about filing tax returns and other matters.

Please send your protest statement, Form 2848 and any supporting documents to this address:

You may also fax your statement using the fax number shown in the heading of this letter. If you fax your statement, please call the person identified in the heading of this letter to confirm that he or she received your fax. If you have any questions, please contact the person whose name and telephone number are shown in the heading of this letter.

Sincerely,

Robert Choi
Director, Exempt Organizations
Rulings & Agreements